

**STATE BOARD OF ACCOUNTS**  
**302 West Washington Street**  
**Room E418**  
**INDIANAPOLIS, INDIANA 46204-2765**

REVIEW REPORT  
OF  
STATE PERSONNEL DEPARTMENT  
STATE OF INDIANA  
March 1, 2000 to February 28, 2003





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AGENCY OFFICIAL

Office

Official

Term

Director

Ms. D. Sue Roberson

01-13-97 to 01-10-05



# STATE OF INDIANA

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## INDEPENDENT ACCOUNTANT'S REPORT

TO: THE OFFICIALS OF THE STATE PERSONNEL DEPARTMENT

We have reviewed the receipts, disbursements, and assets of the State Personnel Department for the period of March 1, 2000, to February 28, 2003. The State Personnel Department's management is responsible for the receipts, disbursements, and assets.

Our review was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. A review is substantially less in scope than an examination, the objective of which is the expression of an opinion on the receipts, disbursements, and assets. Accordingly, we do not express such an opinion.

Financial transactions of this office are included in the scope of our audits of the State of Indiana as reflected in the Indiana Comprehensive Annual Financial Reports.

Based on our review, nothing came to our attention that caused us to believe that the receipts, disbursements, and assets of the State Personnel Department are not in all material respects in conformity with the criteria set forth in the Accounting and Uniform Compliance Guidelines Manual for State Agencies, and applicable laws and regulations except as stated in the review comments.

STATE BOARD OF ACCOUNTS

August 5, 2003

STATE PERSONNEL DEPARTMENT  
REVIEW COMMENT  
February 28, 2003

FLEXIBLE SPENDING ACCOUNTS

What Is Flexible Spending?

A Flexible Spending Account is a type of cafeteria plan authorized under Section 125 of the Internal Revenue Code. Flexible spending accounts allow employees to choose certain qualified benefits in exchange for reduction in salary. These benefits are not considered income and so are income tax free. The State of Indiana offers two qualified benefit plans, medical and dependent care. An employee may participate in either or both of these plans.

To participate, the employee must estimate the dollar amount in claims that he or she will submit for the plan year. This is the election amount. The election amount is then divided between the number of pay periods during the plan year. The result is the amount that the employee agrees to have deducted from their salary each pay period. Once authorized, the employee cannot elect out during the plan year unless certain qualifying events occur. The employee must submit a new election for each new plan year. An election will not carry forward from one plan year to the next. The medical and dependent care plans are considered separate. If an employee is in both, the employee may not use contributions for one plan to supplement payment of claims from the other.

There are certain risks to both the State and the employee. The employee is allowed to make qualified claims up to the total election amount. However, if the employee does not claim against the entire election amount the difference is forfeited to the plan. The State then has the choice to retain, return to participates as premium refund, or reduce required premiums for the following year. A refund or reduction of premium must be made on a uniform basis across participation and not based on an individual's claim history.

The State has risk arising from the health plan. The total election must be made available to the employee at the beginning of the plan year. If the employee resigns or is terminated during the plan year the employee no longer is required to contribute to the plan. However, the plan must pay for those health care claims arising from services provided prior to the employee's separation. This means that the employee may lay claim to the entire election amount without making all of the expected contributions.

Administration of the Flexible Spending Accounts

The Department of Personnel is responsible for the administration of the flexible spending accounts. This includes plan creation, policy determinations, contracting, and monitoring. The State executed a contract with Anthem Insurance Co. to act as the third party administrator (TPA) for these accounts. Anthem then entered into a subcontractor relationship with FlexBen Corporation to perform the TPA responsibilities.

Process for the Flexible Spending Accounts

The employee submits to their individual agency's payroll clerk a Flexible Benefit Election/Change Form. This form authorizes both the type of election and amount of the election. Based on this information, the payroll clerk fills out a Universal Payroll Authorization form (AS-47) and has the employee sign. The AS-47 is submitted to the Auditor of State to authorize the payroll deduction.

The Auditor of State sends to FlexBen a detail of flexible spending deductions for each pay period. FlexBen multiplies the initial deduction for an employee's flexible spending, as indicated by records sent by the Auditor of State, by the number of pay periods in the plan year. This is the amount used by FlexBen as the total election amount that an employee may claim against but not go over.

STATE PERSONNEL DEPARTMENT  
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February 28, 2003  
(Continued)

An employee submits appropriate claims directly to FlexBen. FlexBen issues a check to the employee. FlexBen requests from Anthem reimbursement for checks issued to employees. Anthem bills the State for FlexBen requests and administrative fees. FlexBen sends to employees quarterly reports of activity detail for their accounts. FlexBen also makes available to the Department of Personnel certain reports including the forfeiture report.

Findings

We reviewed the forfeiture report provided and found certain anomalies. For example, there appeared to be a significant number of employees who had exceeded the amount deducted, an instance where the total election amount exceeded the \$5000 maximum, several instances where the year to date deposit exceeded the total election, names that were incomplete, rounding done on some amounts and not on others, and an instance where there was no election amount but there was a deposit amount. We then compared to the Auditor of State's records and found other causes for concern. For example there were instances where the amount deducted exceeded the election amount indicated on the forfeiture report and that amount exceeded was shown as forfeited. Also, there were instances where the amount shown on the forfeiture report was less than the amount shown as deducted by the Auditor of State. Finally, we also requested some Flexible Benefit Election/Change Forms. We found instances where the authorized amount on the election form did not agree with the election amount on FlexBen's report. We also found instances where the election form had not been maintained by the agency.

Our concerns on these and other issues were brought to the attention of the Department of Personnel. They did detailed research for plan years from 1999 through 2002 (prior to 1999 documentation was not available from the TPA). They found a wide range of causes for the anomalies that we noted. For example, for the plan year July 1999 through June 2000 it appears that deductions were made that had not been authorized for the new plan year but were a continuation of the prior plan deduction. These were found early in the year and the deductions stopped. However, FlexBen calculated election amounts based on the initial deduction and it appears that some employees made claims up to the election amount. There were other cases where the initial deduction amount was not the same as subsequent deductions. Again, it appears that FlexBen used the initial deduction and that this resulted in incorrect calculations of election amounts. When a calculation resulted in a higher election amount than the intended election amount the employees were allowed to claim more than their actual approved deductions. Conversely, when the initial deduction calculation resulted in an election that was less than the intended election, the employee could not claim the full amount that was deducted. It also appears that there were calculation errors in 2002 resulting from changes from twenty-six pay periods to twenty-seven pay periods.

Identified errors resulted in overpayments to FlexBen in the amount of \$7200.71. Reimbursement was requested and received (See Summary, Page 9).

The Department of Personnel was not able to complete research on all anomalies noted. Records were often incomplete and the time involved to determine cause for each issue was very time consuming. Personnel is still researching the proper resolution for those employees who may have been under or over reimbursed.

Internal Control Weaknesses

We found various internal control weaknesses that contributed to the anomalies noted in the flexible spending plan. These included:

STATE PERSONNEL DEPARTMENT  
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February 28, 2003  
(Continued)

1. No verification system was in place to ensure that the election authorized by the employee on the Flexible Benefit Election/Change Form was the election amount utilized by FlexBen.
2. No verification system was in place that verified that the deduction amount in the Auditor of State's system agreed with the election amount.
3. No requirements existed for the consistent treatment of calculating the pay period amounts by the payroll clerks. This resulted in rounding issues.
4. No statewide policy existed on how the Flexible Benefit Election/Change Form is to be maintained.
5. No monitoring existed of account activities as submitted by FlexBen. This included reconcilements between the Auditor of State records and FlexBen records, verification that the employees existed, status of employees, or that activity was reasonable.
6. Claims received by Personnel for flexible spending from the TPA did not identify the plan year the reimbursements were for. Without knowing how much the State expended for a given plan year, Personnel was not able to determine the total amount of forfeiture or State liability for a plan year.

Additionally we found that:

1. An option had not been selected for forfeitures. As noted above the State has the option to retain the forfeitures (which should be submitted to the general fund), return the forfeitures to the group of participants as premium refund, or reduce required premiums for the following year. Since the Department of Personnel has not been tracking the balance of payments for each plan year and there are outstanding issues to be resolved, it is not know if there will be a forfeiture balance. However, the fund center indicates a balance and the insurance industry has advertised that normally these plans result in a forfeiture balance. Once it is determined what, if any, forfeiture balance remains, the Department of Personnel should implement the option selected.
2. The Department of Personnel has not addressed payment into the flexible spending plans for those employees who have not had a payroll deduction due to being on unpaid leave or disability.
3. Continuation of flexible spending was not offered to those eligible for COBRA.

Each agency, department, institution or office should have internal controls in effect which provide reasonable assurance regarding the reliability of financial information and records, effectiveness and efficiency of operations, proper execution of managements' objectives, and compliance with laws and regulations. (Accounting and Uniform Compliance Guidelines Manual for State Agencies, Chapter 1)

Each agency is responsible for maintaining an effective and accurate accounting system for subsidiary and supplementary records. At all times, the agency's manual and computerized records, subsidiary ledgers, control ledger, and Auditor's balance should agree. (Accounting and Uniform Compliance Guidelines Manual for State Agencies, Chapter 1)



STATE PERSONNEL DEPARTMENT  
EXIT CONFERENCE

The contents of this report were discussed on February 26, 2004, with Ms. D. Sue Roberson, Director. The official response has been made a part of this report and may be found on Pages 8.



JOSEPH E. KERNAN, Governor

D. Sue Roberson, Director  
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March 5, 2004

Mr. Charles Johnson, State Examiner  
Indiana State Board of Accounts  
302 West Washington Street, Room E418  
Indianapolis, Indiana 46204-2738

Official Audit Response

Dear State Examiner Johnson:

Thank you for the efforts expended by the State Board of Accounts in the audit covering March 1, 2000 through February 28, 2003. We are gratified that, for the three year period under examination, only a single program warranted a review comment.

FlexBen, the flexible spending accounts administrator, has been replaced by Key Benefit Administrators and the full amount in dispute (\$7210.71) has been refunded to the State. In response to the internal control weaknesses, which contributed to the delay in discovering the anomalies, the following changes are being or have already been instituted:

- 1) The new administrator has been instructed to enter into their system the election amount directly from the participant's application. In future plan years, annual election amounts should be transmitted electronically from the Peoplesoft Benefits Module to the third party administrator (TPA).
- 2) The State Personnel Department will compare the enrollment information in the Peoplesoft Benefits Module, the TPA's system, and the Auditor of State's Payroll System to insure that:
  - Annual election amounts are the same in the three (3) systems.
  - Annual election amounts do not exceed the plan limit.
  - Bi-weekly payroll deductions will equal the annual election amount.
  - Information exists in the three (3) systems for all participants.
- 3) Payroll Clerks will be instructed to round deduction amounts up, identify the election amount as the deduction limit and thereby cause the Auditor's payroll system to stop or adjust the deduction amount, once the limit has been met.
- 4) Open enrollment communications issued each year and the Benefits Manual instruct payroll clerks to maintain copies of benefit election forms in the employee's file.
- 5) Ongoing comparisons between systems will identify potential participation problems.
- 6) State Personnel will perform plan year reconciliations to ensure accuracy in the reported amounts of forfeitures and overpayments by the TPA.
- 7) Employees on leave without pay will have their eligibility to participate in the program suspended. Upon return to pay status, the bi-weekly deduction will be recalculated to meet the annual election amount.
- 8) Continued participation in the flexible spending accounts will be offered to those eligible through COBRA.
- 9) Unless otherwise directed by the State Budget Agency, forfeitures will continue to be retained by the State.

We commend Jaspal Singh, Debra Gibson and Mike Hoose for their courtesy, professionalism, and cooperative assistance throughout this audit process. It has improved administration of the flexible spending accounts program. We appreciate and invite your continued participation to ensure that proper methods, standards and procedures are being employed in all of our accounting systems.

Sincerely,

D. Sue Roberson, Director

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STATE PERSONNEL DEPARTMENT  
SUMMARY

	<u>Charges</u>	<u>Credits</u>	<u>Balance Due</u>
Anthem Insurance Co., and FlexBen Corp., Jointly and Severally	\$ 7,200.71	\$	\$
Payment Received Check No. 21013, Dated February 5, 2004		4,313.15	
Credit on Invoice AFA30002220-8, Dated April 21, 2004		<u>2,887.56</u>	<u>-</u>
Totals	<u>\$ 7,200.71</u>	<u>\$ 7,200.71</u>	<u>\$ -</u>